

This letter describes the application of the Manufacturing Machinery & Equipment exemption to various types of equipment used in an on-line embroidery manufacturing process. See 86 Ill. Adm. Code 130.330. (This is a PLR.)

July 7, 2000

Dear Xxxxx:

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200 (see <http://www.revenue.state.il.us/legalinformation/regs/part1200>), is in response to your letters of March 21 and April 18, 2000. Those letters were a follow-up to the Private Letter Ruling which we issued to you on March 3, 2000. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

In your letter of March 21, you have stated and made inquiry as follows:

According to your Letter, you have based the ruling on your understanding of our integrated manufacturing process as explained to you via a teleconference and our previous letter. The purpose of this communication is to provide updated information as to specific exempt computers and to provide clarification to certain points in your Letter.

UPDATED INFORMATION

On Page 7 of your letter dated March 3, 2000 (hereafter referred to as 'the Letter')(paragraph 3):

Eight of the computers are used exclusively to digitize the image which will be imprinted upon the garment.

Upon further review and based on your commentary, we have determined that there are 4 (not 8) computers dedicated to this process. In addition, that process utilizes a BRAND server and certain TYPE equipment (TYPE equipment) that allows the computers to communicate with the embroidery machines via POWER, which we also believe to be exempt.

Next, with respect to the TITLE operations, COMPANY has recently purchased new state-of-the-art TITLE machines which will allow for computers to electronically store machine settings for repeat orders. Accordingly, when a repeat order is placed, the computer stored settings will automatically pre-set the TITLE machines, eliminating the need for manual operator entry of that information. For that reason, the 2 computers purchased to facilitate the machine presets should also be exempt.

CLARIFICATION

On page 7 of the Letter (paragraph 3):

You have indicated that these computers, in essence, 'operate' the stitching equipment by triggering and guiding specific embroidery sequences, including the utilization of specific thread and colors as well as placement of the logo on a specific portion of the garment.

The above sentence should be truncated after the word colors. The computers do not 'assign' placement of the logo on the garment during production. The computers do indeed operate the stitching equipment by triggering the sequence and thread. However, placement of the logo is carried out when the garment is 'hooped' and placed on the machines to be sewn.

Further on page 7 (paragraph 3):

Specifically, these eight digitizing computers qualify because they are used primarily to 'operate' exempt machinery and equipment – the embroidery, TITLE or heat-transfer machines – in a CAD /CAM system.

In view of the aforementioned dated information, this section should now read 4 computers, and related server and TYPE equipment. Furthermore, the digitizing computers run only the embroidery machinery. TITLE and heat transfer are separate processes, not driven by the digitizing computers.

The information discussed herein, as well as our oral meeting and previous correspondence with the Department is considered proprietary and confidential. We request, at the conclusion of this process, that our record be sealed.

I hope this additional information provides clarity on our CAD / CAM system. Thank you for your time and cooperation in this matter. We look forward to continuing to work with your Department.

In your letter of April 18, you have stated and made inquiry as follows:

According to our understanding, there are a few outstanding issues that require clarification relative to our fully integrated computer-assisted manufacturing process and certain associated technology implications. The purpose of this letter is to provide the necessary clarification for your records.

AS/400 Equipment

As outlined in your Letter:

The AS/400 system is used to manage the production floor. This system, in a nutshell, monitors the manufacturing process from placement of an order, until the order is shipped out of the system. And, While these computers may be essential to the manufacturing process, especially in a high-tech integrated manufacturing process such as yours, they cannot be said to be used primarily to 'operate' exempt machinery and equipment.

In conjunction with the AS/400, we concur with the conclusions outlined in your Letter. We don't believe that any further clarification on this issue is warranted.

TYPE

As we detailed in our March 21, 2000 response to your Letter, the TYPE equipment allows the BRAND server to communicate with the embroidery machines via POWER which initiate the embroidery process. This TYPE technology is independent equipment that is used 100% in the manufacturing process. This equipment actually triggers the physical embroidery of the logo onto the garment via the embroidery machines. Thus, we believe it to be exempt.

BRAND Server

As detailed in our March 21, 2000 response to your Letter:

In addition, the embroidery process(sic) utilizes a BRAND server and certain TYPE equipment...that allows the computers to communicate with the embroidery machines via POWER, which we also believe to be exempt.

The following serves to clarify the role of the BRAND server in the fully integrated computer-assisted manufacturing process.

For an embroidery order, the image to be embroidered onto a garment is received electronically from the customer and is deployed into the graphics management system (which we detailed to you in our original letter dated January 28, 2000). The approved electronic graphic is manipulated into a digitized file (an electronic file that instructs the needle how to sew on the garment) that then resides in the electronic embroidery network in the BRAND server as a 'digitized logo'. This server is a computer and box, which serves as the data warehouse for the digitized stitch files to reside as it awaits production. At production time, the file is sent from the server to the actual embroidery machine via the TYPE equipment.

Computer Associated with TITLE Machines

As detailed in our March 21, 2000 response to your Letter:

Next, the respect to the TITLE operations, COMPANY has recently purchased new state-of-the-art TITLE machines which will allow for computers to electronically store machine settings for repeat orders. Accordingly, when a repeat order is placed, the computer stored settings will automatically pre-set the TITLE machines, eliminating the need for manual operator entry of that information. For that reason, the 2 computers purchased to facilitate the machine presets should also be exempt.

For further clarification, these two computers purchased to facilitate the machine presets are used 100% in the manufacturing process.

I hope this additional information provides further clarity on our CAD / CAM system. As a reminder, the information discussed herein, as well as our oral meetings and previous correspondence with the Department, is considered proprietary and confidential.

As indicated in our earlier Private Letter Ruling, machinery and equipment used primarily (over 50% of the time) in the manufacturing or assembling of tangible personal property for wholesale or retail sale or lease is exempt from Retailers' Occupation Tax. See the enclosed copy of 86 Ill. Adm. Code 130.330. The manufacturing process is the production of any article of tangible personal property, whether such article is a finished product or an article for use in the process of manufacturing or assembling a different article or tangible personal property, by procedures commonly regarded as manufacturing, processing, fabricating, or refining that changes some existing material or materials into a material with a different form, use, or name. These changes must result from the process in question and be substantial and significant. The exemption would extend to qualifying machinery used by a manufacturer, such as COMPANY, that embroiders or silkscreens apparel, such as t-shirts, uniforms or hats.

Section 130.330(c)(3) describes the application of the manufacturing machinery and equipment exemption to computer-assisted manufacturing systems. The exemption applies to equipment, "including computers used primarily in operating exempt machinery and equipment in a computer-assisted design, computer-assisted manufacturing (CAD/CAM) system."

As we understand the information you have recently submitted, you ask about the applicability of the manufacturing machinery and equipment exemption to three types of equipment. The first two types of equipment are used together to trigger the physical transfer of embroidery onto a garment. This equipment is comprised of TYPE equipment ("TYPE equipment") and a BRAND server. You have indicated that this equipment is used in conjunction with 4 computers that digitize images to be imprinted upon the embroidered garment ("digitizing computers"). As you indicate, these computers actually operate the embroidery machinery. We have previously ruled these computers to be exempt (see our earlier Private Letter Ruling of March 3, 2000). Once a computer has digitized the image, that image resides in an electronic embroidery network maintained by the BRAND server. At

production time, the file containing the digitized image is sent by the server to the embroidery machine. The TYPE equipment and the server work together to allow the digitizing computer to communicate with the embroidery machines via POWER. This communication triggers embroidery of the digitized image onto the garment. Your letter indicates that the TYPE equipment is used "100% in the manufacturing process." We believe that if the TYPE equipment is used primarily in the manner you have described, e.g., to make it possible for the digitizing computer to communicate with and thus operate the embroidery machines, it will qualify for the exemption.

Your letter does not indicate how the BRAND server is primarily used. It would appear that its role in the embroidery process is to send a digitized file to the embroidery machine. The digitizing computer then communicates with the machine through use of the BRAND server and the TYPE equipment, and then operates the embroidery machine. If this is its primary use, we believe that it, too, will qualify for the exemption. However, please note that if the BRAND server is used primarily to transfer information related to job scheduling, inventory control, ordering, accounts receivable or other accounting or managerial functions, it will not qualify for the exemption.

The final type of equipment about which you have inquired is computers used in conjunction with state-of-the-art TITLE machines. These new TITLE machines allow computers to electronically store machine settings for repeat orders. Although not stated in your letter, it is our understanding that these settings control and guide the TITLE process. When a repeat order is placed, the computer-stored settings will automatically pre-set the TITLE machines, thus eliminating the need for a person to input the settings into the TITLE machines. Based upon the limited amount of information provided, it would thus appear that these computers are used to guide and control the TITLE process, i.e., to "operate" the TITLE machines. This being the case, and assuming also that the computers are primarily used in this fashion, we believe that they will qualify for the exemption.

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

I hope this information is useful. If you have further questions concerning this Private Letter Ruling, you may contact me at (217) 782-2844. If you have further questions related to the Illinois sales tax laws, please visit our website at www.revenue.state.il.us or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Jerilynn Gorden
Senior Counsel, Sales & Excise Taxes